

Human Capital Investment and Skill Development

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Unique Aspects of Human Capital

Human capital *is NOT owned by the firm*, and is therefore more prone to under-investment than other forms of intangibles

Human capital *is owned by EMPLOYEES*, which makes the under-investment particularly problematic

From the Perspective of Employees

1. Once a person leaves the formal education system, work is the source of much of their ongoing learning
2. People who benefit from employer-financed education/training enjoy much higher wages (and in all likelihood, less unemployment)
3. Firms' investments in human capital development appear to be lower in the U.S. relative to other developed countries

From the Perspective of Firms

1. Employee mobility undermines firms' incentives to investment in human capital development, relative to other forms of capital
2. For a variety of reasons (including this lack of ownership), firms' investments in human capital development are accounted for as a **cost**
3. These “costs” are not separately reported
4. Hence, firms that make large investments in human capital reporting appear to be “high cost” firms

Evidence of Under-Investment in Human Capital Development

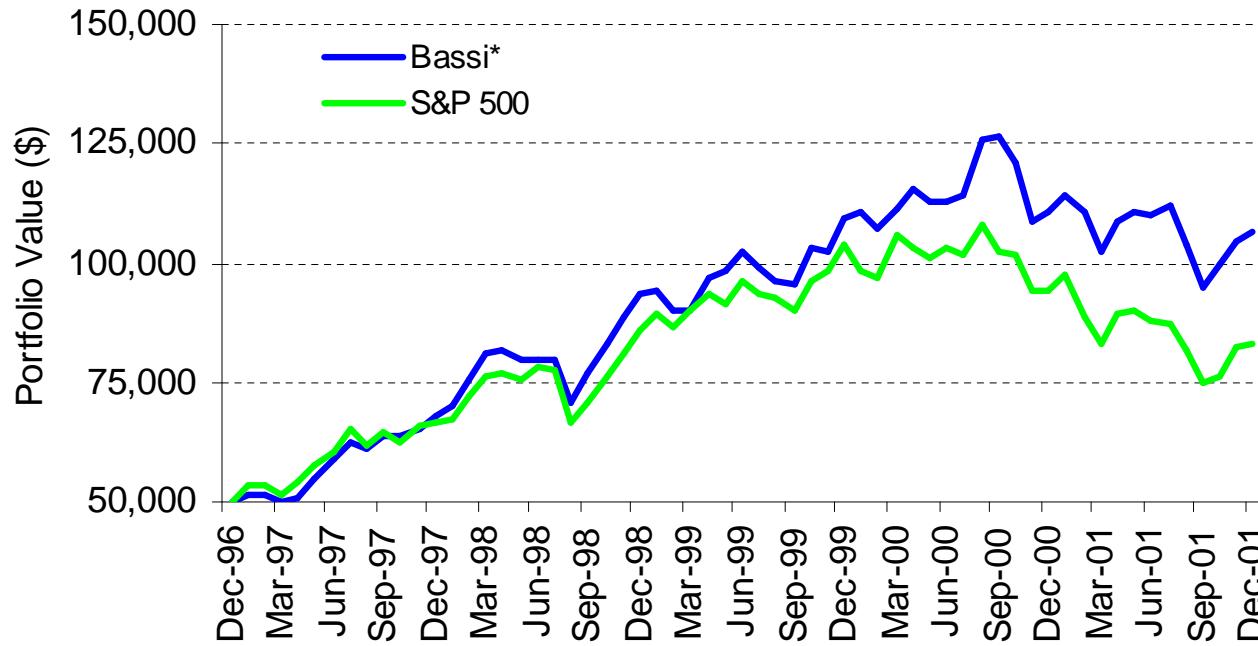
Evidence in this area is hard to come by, precisely because no data are reported

Existing evidence is consistent with under-investment. For example...

1. Very high wage premiums accrue to employees from even modest investments by their employer
2. Out-performance of publicly-traded firms that (appear to) make the largest investment in human capital (education and training)

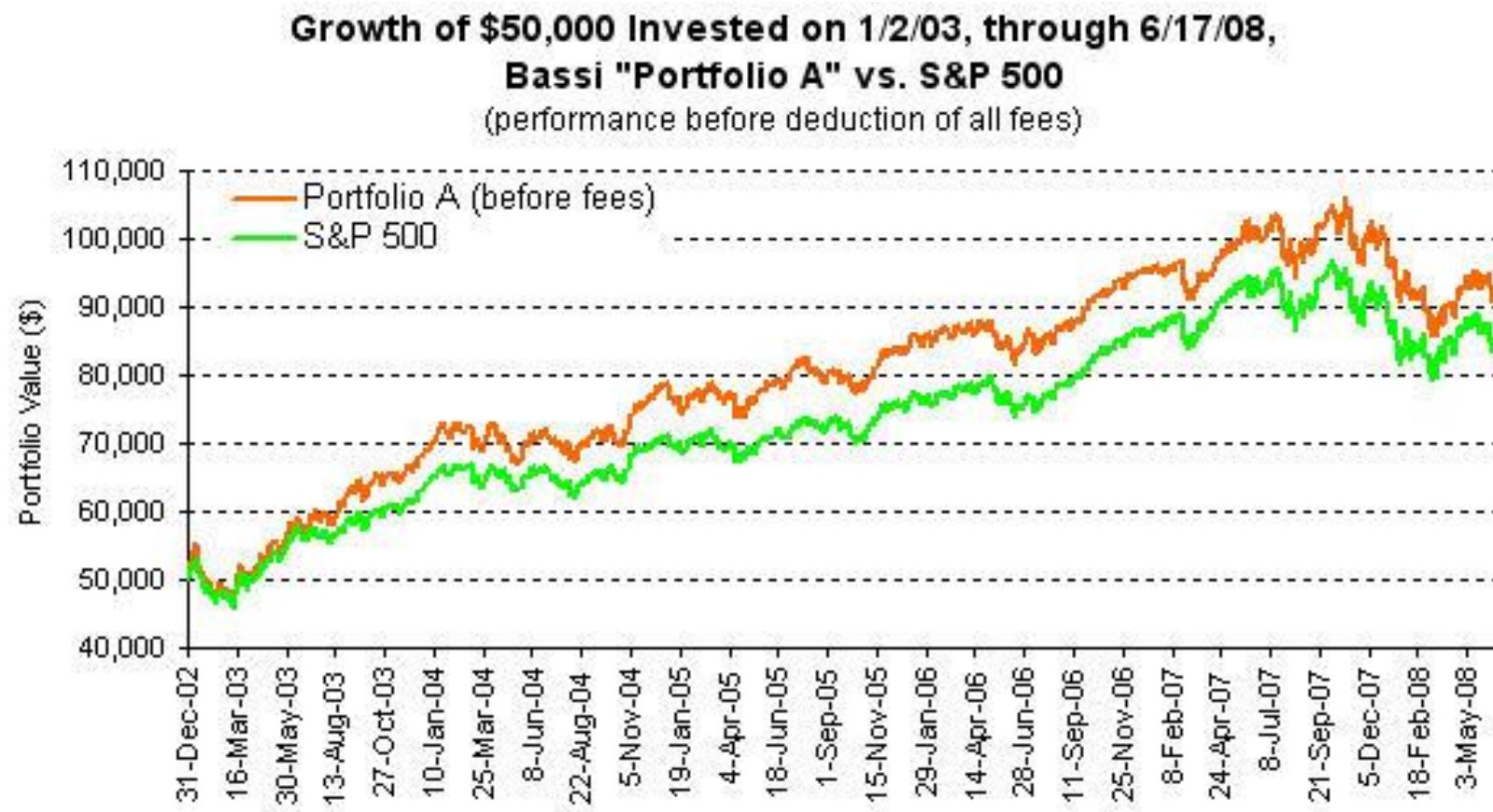
Back-Tested Portfolio of Firms That Make Large Investment in Education & Training

**Growth of \$50,000 Invested on 1/1/97, through 12/31/01,
Bassi Investments Hypothetical Portfolio vs. S&P 500**
(*net performance after dividends and deduction of all fees)



Data represent a hypothetical research-based portfolio and not an active portfolio. Past performance is not a guarantee of future results. For more information, contact Bassi Investments – info@bassi-investments.com.

Actual Portfolio Performance



Source: Bassi Investments.

Conclusions

1. The unique nature of human capital makes it more subject to under-investment than other forms of intangibles
2. The implications of this under-investment are particularly problematic because of their impact on employees (as well as shareholders)
3. Modifying reporting requirements would be an important first step toward correcting this under-investment